

either entity could individually, the Merger also will expedite AT&T's ability to provide content-enriched high-speed Internet cable services.

First, the upgrades that are required to provide local telephone service over cable plant are also necessary to provide cable Internet services over these same facilities. By expediting the rollout of competitive local telephone services, the Merger also hastens the investments necessary for widespread deployment of cable Internet services.

Second, investment by AT&T will spur investment by competitors, and lead them to provide additional services and decrease their prices. The Commission has noted that investment in broadband facilities by cable operators and CLECs "appears to have spurred incumbent LECs to construct competing facilities."⁶⁴ Indeed, this appears to be the case in markets around the country, where ILECs have lowered prices and expanded coverage areas only in response to the entry of substantial competitors.⁶⁵

Video. By enabling AT&T to offer packages of telephone, video, and data services on an expedited basis to millions of American consumers, the Merger will provide

⁶⁴ Report, *Inquiry Concerning the Deployment of Advanced Telecommunications Capability to All Americans in a Reasonable and Timely Fashion, and Possible Steps to Accelerate Such Deployment Pursuant to Section 706 of the Telecommunications Act of 1996*, CC Docket No. 98-146, ¶ 42 & n.84 (FCC Feb. 2, 1999) ("706 NOI Report").

⁶⁵ See, e.g., Mike Farrell, *PacBell to Lower DSL Rates in Calif.*, Multichannel News, November 23, 1998. In other markets where cable operators have initiated broadband service, the incumbent carriers quickly followed suit. For example, @Home launched service in San Francisco in September 1996 and San Diego in May 1997, and Pacific Bell followed in November 1997 and September 1998, respectively. See *Pacific Bell's ADSL-Internet Access Packages Now Available to 180 California Communities* <www.sbc.com/PB/NewsArticle.html?query_type=articlequery=19990901-01>. Likewise, after @Home launched service in Phoenix in May 1997 and Denver in June 1998, US WEST followed in January 1998 and June 1998, respectively. See *US WEST Launches Ultra-Fast DSL Internet Service in Twin Cities; Continues Roll Out* <www.uswest.com/news/051398b.html>.

additional motivation for ILECs and others to step up their efforts to provide competing video programming to end users. The Merger also will accelerate the development and deployment of digital cable technology on MediaOne systems. While AT&T has been a leader in deploying digital technology domestically, MediaOne generally has chosen to focus on increasing the analog capacity of its cable systems. The benefits of digital technology are well known to the Commission. Most importantly, digital technology greatly increases a cable system's capacity and allows the cable operator to bring many more services to consumers, including local and regional programs, niche channels that may be of interest to a small segment of the audience, minority programming, and other diverse services. Digital technology also benefits programmers by creating new opportunities for the distribution of their product.

Clustering. The Merger also serves the public interest by increasing clustering, which will produce pro-competitive efficiencies with regard to all services. As a result of this Merger and the exchange of cable systems with Comcast, AT&T will add network clusters in a number of important service areas. Clustering increases local management, fosters regional programming services, such as enriched local news and sports offerings, enhances compatibility of set-top boxes, lowers maintenance and operating costs, allows more efficient architecture and reduces per-customer marketing costs. Clustering further facilitates the offering of new interactive video services because smaller systems must otherwise bear the cost of either unused file server capacity or use smaller, less efficient servers. Clustering is also essential to the efforts of AT&T to compete with geographically concentrated incumbent LECs because clustering reduces the per-customer cost of providing local telephony. It is precisely for these reasons that

the Commission has concluded that clustering provides significant economic benefits to consumers that outweigh any conceivable harms.⁶⁶

B. These Benefits Cannot Be Achieved Independent Of The Merger

These pro-competitive benefits cannot be achieved on the same scale or as expeditiously absent AT&T's acquisition of MediaOne. As noted above, although MediaOne has begun offering cable telephony in several areas, it has achieved only limited penetration to date and its marketing studies show that consumers remain strongly reluctant to buy telephone service from a cable company. By contrast, for the reasons explained above, combining the complementary assets of AT&T and MediaOne will greatly accelerate and strengthen MediaOne's cable telephony offering.

Similarly, without the transaction, AT&T would be required either to duplicate MediaOne's extensive facilities or to attempt to contract with MediaOne to allow AT&T to lease its facilities to provide cable telephony. The former is economically infeasible, and deprives the public of the benefits in cost reduction and efficiencies generated by the Merger. The latter, as explained below, is, at best, an imperfect solution that would result in much less substantial economic benefits than full integration.

Contractual relationships, even where feasible, are much less efficient than full integration when the parties are trying to deal with rapidly evolving technologies and service.

⁶⁶ Fourth Annual Report, *Annual Assessment of the Status of Competition in Markets for the Delivery of Video Programming*, 13 FCC Rcd. 1034, ¶ 140 (1998) ("Fourth Annual Video Competition Report"); Second Report and Order, *Implementation of Sections 11 and 13 of the Cable Television Consumer Protection and Competition Act of 1992*, 8 FCC Rcd. 8565, ¶ 17 (1993) ("Cable Ownership Limits Order").

This is particularly true where, as here, there is technology and service *convergence* – no one can predict very far into the future what technologies and services are going to develop increased demand and what that means for efficient allocation of cable bandwidth. Without knowing the answers to these questions, potential joint venture partners have difficulty resolving how much bandwidth would be reserved for services to be provided by one joint venturer and how much bandwidth would be reserved for services to be provided by the other joint venturer.

An undefined arrangement in this area is highly problematic because of the large contract-specific investments that must be made early in the project. As noted above, rollout of cable telephony and other cable services requires large initial investments in research and development, licenses and permitting, acquisition of real estate and capital assets, installation of cable and customer premises equipment, marketing and advertising, and staffing of customer care centers. Many of these investments, once made, are contract-specific (they could not be redeployed elsewhere by a party that withdrew from the project) and sunk (they could not be recovered even upon termination of the project). The rapid growth and change in technology and demand for service, the convergence of services, and the high costs associated with initiating service efforts all impact negatively on contractual allocation of the broadband network, especially for new entrants competing against well-established competitors such as ILECs. Accordingly, the most efficient option – the one that promises the most benefits to consumers in the shortest time – is for AT&T and MediaOne to merge and let consumer demand and market forces determine how bandwidth should be used.

V. COMPETITIVE ANALYSIS

The product markets possibly relevant to an analysis of the Merger include: (1) local exchange and exchange access services; (2) domestic long distance services; (3) United States international telephone services; (4) wireless telephone services; (5) multichannel video programming distribution ("MVPD"); (6) video programming; and (7) Internet access.

A. Local Exchange And Exchange Access Services

Residential Telephone Services. The Merger will greatly enhance competition for residential local exchange and exchange access services by enhancing the ability of AT&T and MediaOne to provide facilities-based local telephone service to mass market customers. As the Commission has recognized, "incumbent local exchange carriers are the sole actual providers of local exchange and exchange access services to the vast majority of residential and small business customers in most areas of the United States."⁶⁷ In 1997, ILECs earned more than 98 percent of all local exchange and local exchange access revenues nationwide, with competition from CLECs generally focusing on large business customers in large urban areas.⁶⁸ In February of this year, the Commission estimated that ILECs still earn at least 95 percent of all local exchange and exchange access revenues.⁶⁹ Within the last year, the Commission acknowledged that, regardless of the development of some competition for the largest business customers, it could find little evidence of any actual competition to the ILECs with respect to the provision of

⁶⁷ *AT&T-Teleport* ¶ 21; *see also AT&T-TCI* ¶ 46 (recognizing dominance of ILECs in the provision of mass market telephone service).

⁶⁸ *AT&T-Teleport* ¶ 24 n.80; *1999 Trends* at 9-2.

⁶⁹ *1999 Trends* at 9-1.

mass market local telephone service;⁷⁰ the merger of AT&T and TCI provided the only such hope.

AT&T and MediaOne taken together today provide only a tiny fraction of residential local exchange and exchange access service across the United States. AT&T has approximately 220,000 local telephone service customers throughout the United States, with almost all of those customers receiving resold local ILEC telephone service. While AT&T is in the process of upgrading TCI's cable facilities and initiating new facilities-based local telephone service in service areas like Fremont, California, AT&T has no more than 15,000 such customers in Fremont and San Jose, California; Arlington Heights, Illinois; Dallas, Texas; and Hartford, Connecticut. For its part, MediaOne currently has approximately 26,000 local telephone service customers in Atlanta, Georgia; Boston, Massachusetts; Jacksonville and Pompano Beach, Florida; Detroit, Michigan; Los Angeles, California and Richmond, Virginia. As these figures indicate, AT&T and MediaOne do not currently serve the same service areas or compete with each other in the provision of facilities-based local telephone service in any service area.⁷¹ As a consequence, the proposed Merger will not result in any diminution of competition for local telephone service in the areas served by AT&T and MediaOne.

⁷⁰ *AT&T-Teleport* ¶ 24 n.81. In February of this year, the Commission estimated that CLECs control less than 3 percent of the switched access lines nationwide, and that while CLECs are deploying fiber optic systems, they still only control approximately 11 percent of that capacity. *1999 Trends* at 9-1, 9-2.

⁷¹ AT&T does provide a limited amount of resold local telephone service in Georgia, where MediaOne has initiated local telephony offerings. MediaOne, however, has approximately 5,000 customers in this service area, and AT&T is no longer marketing its resold ILEC local telephony.

Moreover, all of the relevant service areas are dominated by the ILECs, which have considerably more than 90 percent of the customers and revenue in the service areas where MediaOne and AT&T provide local telephone service. Each of the major ILECs with which the merged AT&T-MediaOne will compete has *millions* of customers in these areas. In Georgia, for example, AT&T and MediaOne together serve less than 15,000 local customers through facilities-based service and resale. BellSouth, by contrast, reported more than 4.15 million subscriber lines in Georgia as of the close of 1998, slightly less than 85 percent of all local telephone lines in Georgia.⁷² Almost all of the remaining 15 percent of local telephone lines were held by other incumbent local telephone companies.⁷³ Thus, even where both AT&T and MediaOne have initiated some residential local exchange service, they remain very small, and face a dominant competitor, which has over 100 times as many customers.⁷⁴

As discussed above in Section IV, instead of inhibiting competition, the Merger unquestionably will promote competition in the provision of local residential telephone service in areas where MediaOne has existing network infrastructure. As a result of the Merger, AT&T and MediaOne together will be able to provide more competitive facilities-based local telephone services to more consumers much faster than AT&T or MediaOne independently could provide such service.

⁷² *Trends in Telephone Service*, at 98 (CCB July 1998) (“1998 Trends”).

⁷³ In 1997, 35 other independent local telephone companies reported approximately 700,000 additional lines in Georgia. *Id.*

⁷⁴ Moreover, as the Commission found in *AT&T-TCI*, cable companies like MediaOne have “no special incentives, assets, or capabilities” outside of their cable service areas that would ordinarily suggest that they would compete with AT&T’s current cable telephony efforts in the provision of local telephone service. *AT&T-TCI* ¶ 45.

Business Telephone Services. The Merger also will not impede competition for the provision of local exchange and exchange access services to businesses. As with residential service, the Commission has found that “[i]ncumbent LECs also continue to dominate the larger business market for local exchange and exchange access services.”⁷⁵ AT&T and MediaOne, by contrast, presently provide a very limited amount of local exchange and exchange access services to larger businesses in the United States. Indeed, the ILECs still earn in excess of 90 percent of the business revenues from the provision of local exchange services, and still control approximately nine times the number of fiber miles controlled by new entrants.⁷⁶ AT&T, after its acquisition of Teleport, does seek to compete with the ILECs in the provision of local business telephony, but AT&T’s share of local revenue in business local exchange services has never exceeded four percent in any area.⁷⁷ MediaOne has never been or even sought to be a significant provider of telephony services to businesses.⁷⁸ In Atlanta, for example, where MediaOne currently serves approximately 5,000 local telephony customers, less than 250 of these are businesses.

⁷⁵ *AT&T-Teleport* ¶ 26.

⁷⁶ See *1999 Trends* at 9-2; Table 9.1, Chart 9.1; *AT&T-Teleport* ¶ 27.

⁷⁷ *AT&T-Teleport* ¶ 36.

⁷⁸ TWT, in which MediaOne has a 19 percent interest, has sought to compete as a CLEC in the provision of local business telephone services, but, like other CLECs, has attained only very small shares of that business. For its 1998 fiscal year, TWT earned approximately \$122 million in total revenues from operations in its 20 cities. Time Warner Telecom Prospectus, at 11 (May 11, 1999). Even in the territories where Teleport and TWT both operate as CLECs, their combined market share of local revenue and customers does not exceed four percent and the ILEC competitor still dominates service. Moreover, numerous other CLECs have begun to provide service in these cities. See *AT&T-Teleport* ¶ 27.

Further, even beyond the dominant ILECs, “numerous new entrants are rapidly entering this market, especially in central business districts in urban areas, and . . . any number of these other new entrants have both the capabilities and the incentives to compete effectively.”⁷⁹ These other new entrants will be “at least as significant a competitive force as either of the merging parties.”⁸⁰ The Merger therefore will not significantly affect competition in the provision of local business exchange and exchange access services.

B. Domestic Long Distance Services

The Merger poses no threat to competition in the provision of long distance services because MediaOne is not a competitor for this service. MediaOne does not provide long distance service, and where it provides local telephony, its customers may select a long distance provider from among those companies offering such service. Additionally, as the Commission has recognized, AT&T’s share of long distance services has declined steadily over the past 15 years, justifying AT&T’s reclassification as non-dominant in 1995.⁸¹ As summarized in a recent Commission report, “[s]ince mid-1984, AT&T’s traffic has grown at a slower rate than the industry average: its minutes have doubled during that period while the minutes for other carriers have increased tenfold. As a result, AT&T’s share of long distance access minutes has fallen

⁷⁹ *AT&T-Teleport* ¶ 27. As the Commission recognized in *Teleport*, in AT&T’s top ten service areas there were between five and 12 operational CLECs, including Focal Communications Corp.; Metromedia Fiber Networks; ~~Me~~Tel; RCN Corporation; USN Communications, Inc.; WinStar Communications, Inc., and MCI-WorldCom, Inc. *Id.*

⁸⁰ *Bell Atlantic-NYNEX* ¶ 58; *AT&T-Teleport* ¶ 27. See also *AT&T-TCI* ¶ 50 (combination of a cable firm and AT&T will not eliminate any scarce assets or capabilities).

⁸¹ Order, *Motion of AT&T Corp. to be Reclassified as a Non-Dominant Carrier*, 11 FCC Rcd. 3271, ¶ 1 (1995).

sharply.”⁸² In short, the Merger will have no measurable effect on the vigorously competitive supply of domestic long distance services.

C. International Telephone Service

The Merger likewise will not reduce competition for the provision of international telephone services. As with domestic long distance service, MediaOne is not a participant or a previously precluded competitor for the provision of international telephone service, and AT&T is a nondominant carrier with declining share. Further, the Commission correctly has not considered incumbent cable television operators in general to be significant actual or potential competitors for this service.⁸³

D. Mobile Telephone Service

AT&T, through its subsidiary AT&T Wireless, provides CMRS throughout the United States. AT&T Wireless operates and holds interests in CMRS systems in 26 of the largest 30 service areas in the United States. MediaOne and its subsidiaries do not provide CMRS. MediaOne holds a passive, less than five percent interest in Vodafone, which operates and holds interests in CMRS systems in 22 of the 30 largest service areas in the United States.⁸⁴

⁸² 1999 Trends at 11-1. AT&T's share of long distance operating revenues fell from 90.1 percent in 1984, to 51.8 percent in 1995 when AT&T was declared non-dominant, and still further to 44.5 percent in 1997. Long Distance Market Shares – Fourth Quarter 1998, at 16 & Table 3.2 (CCB March 1999).

⁸³ Bell Atlantic-NYNEX ¶ 87; BT-MCI ¶¶ 82-83.

⁸⁴ Vodafone recently acquired AirTouch. MediaOne had acquired an interest in AirTouch as part of the consideration for the merger with AirTouch of MediaOne's CMRS systems originally acquired from U S WEST.

Given the competitive nature of the CMRS marketplace and the inconsequential level of MediaOne's equity interest in Vodafone, the proposed Merger will not reduce competition in the CMRS marketplace. First, as the Commission has recognized, there are numerous competitors providing CMRS in each service area. "There are now at least five mobile telephone providers in each of the 35 largest Basic Trading Areas (BTAs), and at least three mobile telephone providers in 97 of the 100 largest BTAs in the United States."⁸⁵ In areas where AirTouch and AT&T provide CMRS, there are at least three or four competitors currently providing service.⁸⁶ Moreover, in each service area, there are at least five CMRS competitors licensed to provide service: two cellular providers with at least 25 Mhz are licensed in each cellular service area, and three PCS service providers with at least 30 Mhz are licensed in each PCS service area.⁸⁷ The Merger raises no conceivable consumer harms in the intensely competitive wireless industry.

Second, AT&T's potential indirect ownership of less than a five percent interest in Vodafone is not sufficiently significant to influence the activities of Vodafone. To promote competition and address concerns about anticompetitive behavior among CMRS systems, the Commission has adopted a CMRS spectrum cap that limits the amount of CMRS spectrum that can be held by a single entity in a particular geographic area.⁸⁸ Specifically, Section 20.6 of the

⁸⁵ News Release, *FCC Adopts Fourth Annual Report of State of Wireless Competition*, WT Report No. 99-13 (FCC June 10, 1999).

⁸⁶ See <www.app.airtouch.com/about/cellular_pcs.html>.

⁸⁷ Prior to its merger with Vodafone, AirTouch recognized the potential for up to nine competitors in each of its service areas, including SMR operations and other allocations for PCS. See *id.*

⁸⁸ 47 C.F.R. § 20.6. The CMRS spectrum cap is the subject of a pending rulemaking proceeding. See Notice of Proposed Rulemaking, *1998 Biennial Regulatory Review – Spectrum* (Continued . . .)

Commission's rules (the "Spectrum Cap") prohibits an entity from having an attributable interest in a total of more than 45 Mhz of CMRS spectrum licensed for cellular, broadband PCS, and Specialized Mobile Radio with significant overlap in any geographic area.⁸⁹ Stock ownership is not attributable, however, unless it amounts to 20 percent or more of the equity or voting stock of the CMRS licensee in the service area, or otherwise constitutes control of the licensee.

Because MediaOne's interest in Vodafone is far below the 20 percent attribution level, the proposed Merger will not cause AT&T to violate the Commission's Spectrum Cap. Moreover, MediaOne's interest in Vodafone's CMRS systems has been brought below five percent; MediaOne exercises no control or influence over the domestic operations of Vodafone, and is not involved in the management of Vodafone or its CMRS operations. In fact, MediaOne has "monetized" most of its stockholdings in Vodafone, further reducing any real interest in its CMRS operations.⁹⁰ Given the level of MediaOne's equity interest in Vodafone and its compliance with the Spectrum Cap, no competitive CMRS issues are raised by the proposed Merger.⁹¹

(... Continued)

Aggregation Limits for Wireless Telecommunications Carriers, WT Docket No. 98-205 (FCC Dec. 10, 1998) ("*CMRS Spectrum Cap NPRM*").

⁸⁹ 47 C.F.R. § 20.6(a). Significant overlap of a PCS and cellular service area is defined as a ten percent population overlap. *Id.* § 20.6(c)(1).

⁹⁰ A "monetization" is a transaction that permits a company to capture the value of the gains of an appreciated asset, such as common stock of another company that it owns, while deferring the capital gains that would accompany an outright sale. MediaOne has monetized more than two-thirds of its Vodafone shares and it is in the process of monetizing the remaining shares. Thus, while MediaOne continues to own these Vodafone shares, much of the economic interest in these shares has been transferred to other investors.

⁹¹ AT&T may require a temporary waiver of Section 22.942 of the Commission's rules if Section 22.942 remains in effect. Section 22.942, which was adopted before the Commission's allocation of spectrum for PCS, when there were only two cellular licensees in each market,
(Continued...)

E. Multichannel Video Programming Distribution

AT&T's acquisition of MediaOne will not eliminate or reduce competition in the MVPD marketplace. With very minimal exception, there is no geographic overlap between AT&T's cable systems and MediaOne's systems.⁹² Applicants currently believe that, among the territories in which both AT&T and MediaOne have authority to offer cable service, the only actual overbuilds are in discrete sections within the Atlanta, Georgia MSA (Powder Springs, Fayetteville, Fulton County and Peachtree City).⁹³ In total, it appears that fewer than 3,000

(... Continued)

prohibits an entity from having an ownership interest in licensees for both channel blocks in overlapping cellular service areas unless the interests pose no substantial threat to competition. 47 C.F.R. § 22.942. AT&T Wireless and Vodafone have interests in both channel blocks in 37 cellular service areas in California, Colorado, Idaho, Minnesota, Nevada, Oregon, Utah, and Washington.

In adopting Section 22.942, the Commission determined that interests of less than five percent would not implicate the rule in circumstances where control was not present. *Id.* § 22.942(a). MediaOne's interest in Vodafone does not convey any rights to influence, much less control, Vodafone. In addition, now that Vodafone has acquired AirTouch, MediaOne's passive investment in Vodafone still will not pose any threat to competition, much less a substantial threat. As part of its *CMRS Spectrum Cap NPRM*, the Commission is reconsidering the continued need for Section 22.942. Since Section 22.942 was adopted, the Commission has allocated an additional 120 Mhz for PCS services and adopted rules that permit SMR operators to provide CMRS services that also compete with cellular services. In such circumstances, it is difficult to reconcile the Spectrum Cap limit of 20 percent, which permits ownership in overlapping PCS and cellular systems, with a different limit that would prohibit ownership of less than a 5 percent interest in overlapping cellular systems. If a waiver is necessary, AT&T would commit to bring itself into compliance with whatever rule is adopted by the Commission in the *CMRS Spectrum Cap NPRM* proceeding.

⁹² The analysis in this section focuses on cable systems in which AT&T or MediaOne have a 50 percent or greater ownership interest.

⁹³ Other than in the Atlanta service areas, AT&T and MediaOne each hold franchises to operate cable systems in common territories within seven service areas: Riverside-San Bernardino, California; Peoria-Pekin, Illinois; Ann Arbor, Michigan; Miami, Florida; Chicago, Illinois; Kankakee, Illinois, and Lansing/E. Lansing, Michigan. However, proposed exchange transactions between AT&T and MediaOne that will eliminate the overlaps in Miami, Chicago, Kankakee, and Lansing/East Lansing have already been cleared by the antitrust authorities, (Continued...)

homes in those franchise areas have actually been overbuilt. Given this insignificant degree of overlap, a combination of AT&T and MediaOne would have at most a *de minimis* impact on MVPD competition and clearly would pale in comparison to the substantial public interest benefits and efficiencies to be realized by the Merger, including the acceleration of local telephony competition.⁹⁴

In fact, the Merger likely will *increase* MVPD competition. By enabling AT&T to provide packaged (as well as separate) voice, video, and Internet services to millions of American consumers on an expedited basis, the Merger will increase the incentive of local telephone companies and others to compete in the provision of multichannel video services. In such an environment, ILECs and others will be motivated to upgrade their networks to enable them to provide comparable packages that include video programming as well as other types of services. Indeed, there already is evidence that AT&T's plans to provide service packages are causing ILECs to seek ways to offer multichannel video services along with their traditional telephony services. For example, both SBC and Bell Atlantic have partnered with DirecTV to

(... Continued)

pursuant to the Hart-Scott-Rodino Antitrust Improvements Act of 1976 ("HSR Act"). The required HSR notification (Transaction No. 19990624) was filed on November 25, 1998, and the waiting period expired on December 25, 1998. Similarly, MediaOne has entered into definitive agreements for transfers to Time Warner that will eliminate overlaps with AT&T in Riverside-San Bernardino, with the exception of franchise territories in which there is no overbuild. These transfers also have received clearance under the HSR Act. The HSR notification (Transaction No. 19991719) was filed on March 1, 1999, and the waiting period terminated on March 31, 1999. The two remaining MSAs known to the parties to contain common territories – Ann Arbor, and Peoria-Pekin – contain no overbuilds.

⁹⁴ See *supra* Section IV for a discussion of the substantial public interest benefits created by the Merger.

offer bundled services to customers throughout their service areas.⁹⁵ The Merger thus should stimulate MVPD competition rather than restrain it.⁹⁶

F. Video Programming

The Merger will have no anti-competitive effects in the thriving video programming marketplace. The Merger will result in little real consolidation of programming interests, and AT&T will, in any event, remain a relatively small video programming player. Nor will the Merger create a video programming *buyer* even remotely large enough to exercise monopsony power or to engage in vertical foreclosure. Finally, the Merger will not result in the violation of any currently effective statute or rule directed at video programming concerns. Applicants recognize, of course, that horizontal cable ownership limit issues are before the Commission in two pending industry-wide proceedings. Applicants analyze below the impact of the Merger under various proposals made in those proceedings and demonstrate why such generic proposals – animated by monopsony power and vertical foreclosure concerns that simply

⁹⁵ *Bell Atlantic Introduces Television Service for Apartment, Condominium, Co-op and Townhouse Residents*, (Sep. 14, 1998) <www.ba.com/nr/1998/Sep/19980914002.html>. See also *Bell Atlantic Brings Its New TV Service to Pittsburgh, Offering Consumers an Alternative to Cable* (May 24, 1999) <www.ba.com/nr/1999/May/19990524004/html>; DirecTV Press Release, *SBC Communications, DirecTV, and USSB Sign Agreements to Offer Digital Satellite TV Service in Apartment Complexes* (Mar. 2, 1998) <www.directv.com/news/swbdeal.html>.

⁹⁶ In fact, it is important to note that, notwithstanding the increased size of various multiple systems operators (“MSOs”) as a result of the mergers and clustering in the cable industry over the last few years, none of this activity has slowed the growth of cable competitors or diminished competition in the MVPD marketplace. To the contrary, MVPD competition has *increased* during this period. In part, this is because DBS operators, telephone companies, and other MVPDs are responding to the increased investment by cable MSOs in programming, additional channel capacity, and expanded network size. This evidences the true competition existing in the marketplace.

are not present here – should pose no obstacle to expeditious approval of the proposed Merger and the resulting transfer of control of FCC authorizations and licenses.

1. The Merger will have No Adverse Effects on Competition in the Provision of Video Programming

For a variety of reasons, the Merger will not significantly increase concentration in the ownership of video programming and therefore will have no adverse effects on competition in the video programming marketplace.⁹⁷

First, as shown above, the structural and operational separation between Liberty and AT&T means that the Merger does not result in a combination of the Liberty and MediaOne programming interests. To the contrary, after the Merger, the programming interests of Liberty will be controlled and managed entirely separately from the MediaOne programming interests held by AT&T.⁹⁸

Second, following the Merger, AT&T will have a purely passive 25.51 percent limited partnership interest in TWE. AT&T will have no input into the management of the TWE cable systems or the TWE programming interests.⁹⁹

Third, with regard to the remaining programming services to be combined by the Merger (except two regional programming services, New England Cable News and Fox Sports

⁹⁷ The programming interests of AT&T and MediaOne are described above in Section II.

⁹⁸ It is important to stress that AT&T's interest in Liberty, Liberty's ownership interest in Time Warner, Inc., and AT&T's interest in Cablevision/Rainbow were all before the Commission when it addressed the AT&T-TCI merger, and the Commission found no adverse competitive impact on the video programming marketplace.

⁹⁹ See *infra* Section II(B).

New England in which AT&T has a 50 percent interest), AT&T will have only a minority (in some cases very small), indirect interest, with neither control nor management rights. The combination of these interests simply is not significant enough to create a concern about a material increase in the concentration of the programming marketplace.

Fourth, competition in the video programming business is thriving. The Commission has identified 245 national satellite-delivered video services,¹⁰⁰ many of which are owned by large, well-funded, and experienced media companies, such as Disney, Viacom, and NBC. The combination of the limited programming interests held by AT&T and MediaOne will not materially affect competition in such a highly competitive and robust marketplace.

2. AT&T-MediaOne will have No Ability to Exercise Monopsony Power or Engage in Vertical Foreclosure

AT&T will have no ability, after the Merger, to engage in vertical foreclosure or to exercise monopsony power over video programming services. As an initial matter, existing and growing competition from non-cable MVPDs, which serve as alternative outlets for video programming, constrains the ability of *any* multiple system operator ("MSO") to engage in such conduct.¹⁰¹ And, post-Merger, AT&T will control programming decisions or purchase

¹⁰⁰ Fifth Annual Report, *Annual Assessment of the Status of Competition in Markets for the Delivery of Video Programming*, 13 FCC Rcd. 24284, ¶ 159 (Dec. 23, 1998) ("*Fifth Annual Video Competition Report*").

¹⁰¹ See generally Stanley Besen and John Woodbury, "An Economic Analysis of the FCC's Cable Ownership Restrictions," at 5 (Aug 14, 1998) ("Besen and Woodbury") (attached to Comments of TCI, *In the Matter of Implementation of Section 11(c) of Cable Television Consumer Protection and Competition Act of 1992 – Horizontal Ownership Limits*, MM Docket No. 92-264 (Aug. 14, 1998)) ("TCI Ownership Limit Comments") ("[T]he ability to wield buyer power is diminished by the availability of alternative distribution outlets to which program suppliers can turn if a single cable operator, or a collection of operators, were to attempt to
(Continued . . .)

programming for a share of total MVPD subscribers that is far too small to support any plausible argument that AT&T could engage in such conduct.

a. Competition from alternative MVPDs constrains the ability of any MSO to engage in vertical foreclosure or exercise monopoly power

Today, consumers can choose from a variety of multichannel video providers, including DBS, telephone companies, C-Band, multichannel multipoint distribution services ("MMDS"), Satellite Master Antenna Television Systems ("SMATV"), and utilities. More than 12.5 million consumers, representing approximately 16 percent of all MVPD subscribers, now obtain multichannel video programming from some company other than their local cable operator, and more can potentially do so.¹⁰² This non-cable video competition means not only additional choices for consumers but additional outlets for video programmers, the existence of which necessarily constrains the ability of any MSO to exercise monopsony power or to engage in vertical foreclosure.¹⁰³ In the MVPD business, there are numerous actual and potential video

(... Continued)

exercise such power. In particular, the rapid growth of DBS provides program suppliers with an increasingly important alternative to cable operators for the sale of their services."); *id.* at 8 ("[T]he effectiveness of a foreclosure strategy is further weakened if other distributors can carry a rival service the MSO tried to foreclose. In light of developments that have occurred since the passage of the 1992 Cable Act and the adoption by the Commission of rules limiting the size of MSOs – especially the rapid growth in the number of subscribers served by DBS operators – this factor places an especially important constraint on the ability of a large vertically integrated MSO to foreclose a rival program service.").

¹⁰² Order and Authorization, *Tempo Satellite, Inc., Assignor and DirecTV Enterprises, Inc., Assignee*, IBFS File No. SAT-ASG-19990127-00014, (FCC May 28, 1999) ("*Tempo Authorization*").

¹⁰³ See *Fourth Annual Video Competition Report* ¶ 150 ("[a]s non-cable MVPD subscribership increases, the significance of DBS, MMDS, and SMATV operators in the MVPD purchasing (Continued...)")

programming buyers that currently would be “at least as significant a force” as the combined AT&T-MediaOne.

The growth of cable’s competitors has been steadily increasing for several years. For example, in its 1998 annual report on the status of competition in the video marketplace, the Commission noted that the number of subscribers to non-cable MVPDs grew 18 percent between June 1997 and June 1998, while cable subscribership grew by only two percent over the same period.¹⁰⁴ Industry analysts expect this trend to continue and have estimated that the number of non-cable MVPD subscribers will reach 17.8 million, or approximately 22 percent of all MVPD subscribers, by next year.¹⁰⁵

DBS. DBS is a formidable competitor in the MVPD marketplace, offering over 200 channels that include all the most popular and widely carried national cable networks, as well as some programming (such as DirecTV’s exclusive sports packages) that is not available to local cable systems. In addition, the up-front consumer equipment costs for DBS have plummeted from \$700 five years ago to little or nothing today. As the Department of Justice has observed:

Cable and DBS are both MVPD products. While the programming services are delivered via different technologies, consumers view the services as similar and to a large degree substitutable. Indeed, most new DBS subscribers in recent years are former cable subscribers who either stopped buying cable or downgraded their cable service once they purchased a DBS system.¹⁰⁶

(... Continued)

marketplace also increases . . . thus reducing cable operators’ market power or influence in the purchase and distribution of network programming.”).

¹⁰⁴ *Fifth Annual Video Competition Report* ¶ 8.

¹⁰⁵ See, e.g., *Cablevision Bluebook, Volume IX*, at 10 (Summer/Fall 1999).

¹⁰⁶ Complaint, *United States v. Primestar, Inc.*, No. 1:98CV01193, ¶ 63 (D.D.C. May 12, 1998).

More recently, the Commission concluded, “*DBS operators and cable operators have engaged in increasingly rivalrous behavior, and . . . will likely increase the degree of that competition.*”¹⁰⁷

The following additional facts about DBS further highlight that DBS operators are a significant outlets for video programmers:

- Two out of every three new MVPD subscribers choose a DBS operator over the local cable operator as their video programming provider;¹⁰⁸
- Last year, DBS subscribership grew by 43 percent -- over 20 times faster than cable’s subscribership growth during the same period;¹⁰⁹ and
- DBS operators have more subscribers than most cable companies they challenge. DirecTV (with 7.2 million subs) is now comparable in size to the third largest cable MSO; Echostar (with 2.4 million subs) is now comparable in size to the seventh largest cable MSO.

Various industry and regulatory developments will further enhance the competitive strength of DBS. First, DBS providers have begun to partner with other powerful companies in order to establish a presence in local communities and to enhance their service offerings. For example, DirecTV has signed marketing and distribution agreements with both Bell Atlantic and SBC to bundle telephone and video services to consumers.¹¹⁰ Likewise, Echostar has signed strategic partnership agreements with private cable and competitive

¹⁰⁷ Order and Authorization, *MCI Telecommunications Corp. and Echostar 110 Corp.*, FCC 99-109, ¶ 19 (FCC May 19, 1999) (emphasis added) (citing DOJ’s comments filed in that proceeding) (“*Echostar Order*”).

¹⁰⁸ *Fifth Annual Competition Report* ¶ 62.

¹⁰⁹ *Id.* ¶ 12.

¹¹⁰ DirecTV News Release, “SBC Communications, DirecTV and USSB Sign Agreements to Offer Digital Satellite TV Service in Apartment Complexes,” March 2, 1999, <www.directv.com/news/swbdeal.html>; DirecTV News Release, “Bell Atlantic, DirecTV and USSB Announce Agreements,” March 2, 1999 <www.directv.com/news/badeal.html>.

residential phone service providers to bundle Echostar's satellite programming with other services, such as Internet access, telephony, and traditional cable television.¹¹¹

Second, DirecTV recently acquired the United States Satellite Broadcasting Company ("USSB") and PRIMESTAR, which will add a significant number of new subscribers to DirecTV's totals.¹¹² More recently, the Commission approved the transfer of DBS licenses from Tempo to DirecTV, which will enable DirecTV to operate DBS satellites from three orbital locations that are capable of transmitting DBS signals to all portions of the U.S.¹¹³ Indeed, the Commission justified its approval of the Tempo transfer by stating that it will:

allow DirecTV to compete more effectively with EchoStar and cable operators [and] spur technical innovation by encouraging the satellite industry to develop small earth stations that can receive and integrate signals from multiple orbital positions, thus expanding programming choices for DBS subscribers, including under-served consumers.¹¹⁴

Similarly, the Commission noted that its approval of EchoStar's acquisition from MCI of 28 additional DBS channels at the full CONUS 110° orbital slot "will likely allow EchoStar to provide consumers with a more competitive alternative to cable offerings and thereby increase

¹¹¹ Echostar Press Release, "Echostar, OpTel Form Alliance to Provide Dish Network Satellite Television Services to Multi-Family Residential Complexes," February 2, 1999, <www.dishnetwork.com/profile/press/press/press169.html>.

¹¹² DirecTV News Release, "Hughes to Acquire PRIMESTAR," January 22, 1999, <www.directv.com/news/dtvprimestar.html>; DirecTV News Release, "Hughes Completes Acquisition of PRIMESTAR Medium-Power DBS Business," April 28, 1999, <www.directv.com/press/pressdel/0,1112,5,00.html>.

¹¹³ *See generally Tempo Authorization.*

¹¹⁴ *Id.* ¶ 6.

competition in the [MVPD] market, which should lead to additional service offerings and/or lower prices.”¹¹⁵

Finally, Congress’s ongoing legislative initiative to authorize DBS providers to retransmit local broadcast signals within the broadcaster’s local market will further enhance DBS’s competitive significance by eliminating the primary reason why people say they do not subscribe to DBS.¹¹⁶ According to information received by the Commission, 55 percent of individuals inquiring into DBS cited the lack of local broadcast signals as a reason not to purchase DBS.¹¹⁷

ILECs. Ameritech now passes more than 1.7 million homes in Illinois, Michigan, Ohio, and Wisconsin with over 100 cable franchises.¹¹⁸ BellSouth has cable franchises passing 1.2 million homes in parts of the Atlanta, Birmingham, Charleston, and Jacksonville

¹¹⁵ *Echostar Order* ¶ 1.

¹¹⁶ Both the House and Senate have approved bills that would allow satellite carriers to retransmit a local television station to households and businesses throughout that station’s local market, as cable providers do currently. The House bill, H.R. 1554, was approved in April, and the Senate bill, S. 247, was adopted in May. The House and Senate are expected to complete work on the legislation later this summer. Given the pending enactment of this legislation, DirecTV announced plans to offer local broadcast network channels to approximately 50 million homes across the U.S. DirecTV Press Release, *DirecTV Announces Record April Subscriber Growth* (May 12, 1999) <www.directv.com/news/aprilperf.html>. The Commission has also paved the way for direct competition for domestic MVPD service by permitting DBS providers in Mexico and Argentina to provide service in the United States. See Public Notice, *International Bureau Announced Conclusion of U.S.-Mexico Protocol for Direct-to-Home Satellite Services*, 12 FCC Rcd. 13105 (1996); Public Notice, *International Bureau Announces Conclusion of U.S.-Argentina Framework Agreement and Protocol for Direct-to-Home Satellite Services and Fixed-Satellite Services*, DA 98-1114 (FCC June 12, 1998).

¹¹⁷ *Fifth Annual Video Competition Report* ¶ 63.

¹¹⁸ *ANM Launches in Two Ohio Towns*, Multichannel News, at 22 (May 17, 1999). Ameritech bills itself as the nation’s largest competitive cable operator.

metropolitan areas,¹¹⁹ and is a large investor in multichannel multipoint distribution services MMDS.¹²⁰ GTE has cable franchises in California, Florida, and Hawaii, that pass over 500,000 homes.¹²¹ SNET has acquired the first state-wide cable franchise in Connecticut and is offering cable service in over a dozen communities.¹²² U S West operates video systems in Omaha, Nebraska, and Phoenix, Arizona, the latter representing the first use of very high-speed digital subscriber line (“VDSL”) technology to deliver video, high-speed Internet access, and telephone service over existing copper plant.¹²³

In fact, the efforts of AT&T and other cable companies to upgrade and expand their networks are actually increasing the level of MVPD competition, as telephone companies seek to respond to cable’s deployment of broadband technology and services. As explained in more detail below in Section V(G), ILECs are rapidly deploying DSL to provide a wide range of bundled broadband services to consumers.

Utilities. Electric utilities are entering the cable business. For example, RCN Corporation now provides bundled phone, video, and Internet-access services in New York, Boston, New Jersey, and Pennsylvania. It already has at least 63,000 video customers in Manhattan and Boston and recently expanded its cable service to Queens. RCN has also built a \$300-million, 350-

¹¹⁹ *Fifth Annual Video Competition Report* ¶ 114. Other sources indicate that BellSouth passed 1.2 million households as early as August, 1997. See *Wireless Ops Oppose Nets’ Program Access*, Multichannel News, at 35 (Aug. 25, 1997).

¹²⁰ *Fifth Annual Video Competition Report* ¶ 112.

¹²¹ *Does GTE Provide Cable TV?* <www.gte.com/products/prods/americast.html>.

¹²² *Fifth Annual Video Competition Report* ¶ 43.

¹²³ *Id.* ¶ 114.

mile fiber network in the Washington, D.C. region with a local utility, Potomac Electric Power Company, and is already providing similar bundled services under the brand name "StarPower" in the nation's capital.¹²⁴ Similarly, Seren Innovations Inc., a subsidiary of Northern States Power Co., Minnesota's largest electrical and natural gas utility, has begun offering cable and Internet service in Minnesota and has applied for cable franchises in markets served by AT&T in California and Colorado.¹²⁵

Non-Cable MVPDs. While DBS and the delivery of services by telephone companies show the most growth as competitive alternatives to traditional cable companies, other MVPD providers also offer direct competition to cable operators in the MVPD marketplace. For example, C-band distributors serve over 1.8 million subscribers and provide access to several hundred program services.

Moreover, the provision of an additional 6 Mhz of spectrum to local broadcasters to launch digital broadcasting services will "allow broadcasters to become more effective competitors with cable operators in the MVPD market."¹²⁶ In fact, as early as November 1, 1999, more than half of all television households will have access to multiple channels of digital broadcast television.¹²⁷ By combining the digital spectrum of all stations in a local television

¹²⁴ *Id.* ¶ 12.

¹²⁵ *Overbuilder Seren Could Stir Things In Denver*, Multichannel News, at 48 (June 7, 1999).

¹²⁶ *Id.* ¶ 101.

¹²⁷ Notice of Proposed Rulemaking, *Preemption of State and Local Zoning and Land Use Restrictions on the Siting, Placement, and Construction of Broadcast Station Transmission Facilities*, 12 FCC Rcd. 12504, ¶ 2 (1997).

market, broadcasters estimate that they will be able to create a 40 to 50 channel service to compete with existing MVPDs.¹²⁸

In addition, MMDS operators currently serve approximately 1.5 million subscribers, and the Commission reports that the number of homes capable of receiving an MMDS signal grew to 34,000,000 at the end of 1997, an increase of 8 percent over the previous year.¹²⁹ Various companies are already taking advantage of the Commission's recent authorization of two-way digital MMDS¹³⁰ to offer high-speed Internet access, video conferencing, distance learning, continuing education, and other two-way services.¹³¹ As noted by the Commission, its recent *Two-Way Order* provides MMDS operators with greater flexibility to provide service, which will further enhance MMDS' competitive potential.¹³²

SMATV also compete aggressively with cable operators, primarily for multiple dwelling units. There are approximately 1.5 million SMATV subscribers.¹³³ New technological advancements, such as the use of common carrier supertrunking and the integration of DBS and

¹²⁸ *Fifth Annual Video Competition Report* ¶ 101.

¹²⁹ *Id.* ¶ 83.

¹³⁰ Report and Order, *Amendment of Parts 21 and 74 to Enable Multipoint Distribution Service and Instructional Television Fixed Service Licensees to Engage in Fixed Two-Way Transmissions*, 13 FCC Rcd. 19112 (1998) ("*Two Way Order*").

¹³¹ For example, BellSouth and GTE both launched digital MMDS systems in their regions in direct competition with cable operators. *Fifth Annual Video Competition Report* ¶ 81. Once all systems are launched, BellSouth estimates that it will be able to service more than three million homes. BellSouth News Release, *BellSouth Brings New Era of Home Entertainment Service to Atlanta* (June 4, 1998) <www.bellsouthcorp.com/proactive/documents/render/1726.html>.

¹³² *Two Way Order* ¶¶ 8-9.

¹³³ *Fifth Annual Video Competition Report* ¶ 90.